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1

What is the Third Way?

Introduction

The Third Way has been described as arguably ‘one of the most successful theoretical and political strategies’ to have emerged in the contemporary period (Geyer, 2003: 237). Similarly, ‘the debate about the third way has become the most important reform discourse in the European party landscape’ (Merkel, 2001). For supporters, it ‘stands for a modernised social democracy, passionate in its commitment to social justice and the goals of the centre-left, but flexible, innovative and forward-looking in the means to achieve them’ (Blair, 1998d: 1). Moreover, it is portrayed as a form of ‘ethical socialism’ that represents ‘the only serious view of the Left’s future that can remain’ after the substantial changes in the international political economy environment at the cusp of twentieth and twenty-first centuries (Blair, 1994: 3). However, critics contend that the Third Way is in essence an example of Thatcherite revisionism (Hay, 1994, 1999), where principles are abandoned in a cynical attempt to secure political power – in essence, ‘the great moving nowhere show’ (Hall, 1998).

Theorists have described the Third Way as ‘fundamentally vague and elusive’, and may be considered to represent ‘a rhetorically defined space’ rather than an ideology (Lukes, 1999: 3–4; White, 2001: 1). Leading figures associated with the Third Way, including Tony Blair himself, have acknowledged that it should be considered to be a ‘work in progress’, a form of ‘permanent revisionism’ encompassing a perpetual search for improved means to secure ethical goals (Blair, 2001: 2, 4). This emphasises upon the practicality of the Third

Way, but its lack of a well-developed theoretical core, leads Robert Reich to suggest that:

Rarely in the history of world politics has a term gone from obscurity to meaninglessness without any intervening period of coherence. (*New Statesman*, 1 May 1999, cited in Clift, 2004: 36)

One measure of the significance of the Third Way is that it developed at least partly in reaction to a number of recent, substantial developments in the international political economy environment. These include the collapse of what passed for communism in the USSR and Eastern Europe, together with the increasing import of globalisation, the development of flexible-specialisation forms of production and the hegemonic position claimed by neo-liberal economics in the industrialised economies. These events provided a temporary period of euphoria for advocates of the neo-liberal 'new Right', as it appeared to vindicate their treatises against the dangers of communism, and by inference all forms of progressive policies associated with even the mildest form of democratic socialism and/or social democracy. Despite the triumphalism from the political Right, Fukuyama's (1992) announcement of the 'end of history' and the obituaries written for social democracy by Dahrendorf (1988: 140, 172, 1990: 38) and Gray (1998: 89) were, with the benefit of hindsight, rather premature.

A second indication of the importance of the Third Way relates to the electoral success for political parties associating themselves, with varying degrees of enthusiasm, with this form of modernised social democracy. During the five years leading up to 1998, left-of-centre political parties were elected (or re-elected) into government in sixteen out of twenty sets of parliamentary elections held in eighteen west-European countries. Moreover, at the turn of the twenty-first century, social democratic parties were in government, either in coalition or governing on their own, in thirteen out of the fifteen EU member states (Lovecy, 2000: 50, 53). Political commentators were discussing the turnaround in the electoral fortunes of European social democratic parties in similar terms to the rise of the neo-liberal 'new Right' agenda two decades previously (Clift, 2004: 34). Indeed, European social democracy was even voted the 'personality of the year' by the American magazine *Newsweek* in December 1998 (Leonard, 2000: xi).

In Britain, New Labour secured two landslide election victories, whilst Clinton's two-term presidency in the USA overturned twelve years of Republican incumbents. Moreover, the Australian Labor Party had won

five successive General Elections and remained in power between 1983 and 1996. However, whilst this resurgence in democratic left-of-centre electoral fortunes has been described as 'spectacular and unprecedented' in terms of the number of governments formed, this was a slightly misleading indication of electoral strength. Indeed, only two social democratic parties polled more than 40 per cent of the vote (UK and Portugal) in 2000, whilst sister parties in five of the fifteen EU member states polled 20 per cent or less (Sassoon, 1999: 19; Giddens, 2001: 20; Favretto, 2003: 12).

Relative electoral success for social democratic parties, whether or not this proves to be constructed upon weak popular foundations, has certainly stimulated considerable interest in the development of the Third Way. However, it has simultaneously raised a number of fundamental questions relating to the viability of progressive economic policies, the optimum range of policy instruments to be utilised to secure social democratic goals, together with the very nature of social democracy and what it exists to try to achieve. White (2001: x) explains the significance of the evaluation of the Third Way phenomenon in the following terms:

This apparent revival in the fortunes of progressive political parties has generated much excitement. But it has also generated much confusion and debate. In essence, the debate is about the extent to which the electoral success of these notionally progressive political parties really will, or can, translate into a reassertion of progressive values at the societal level. Are we witnessing a political realignment in the advanced capitalist world that will further progressive commitments to social justice (understood in reasonably egalitarian terms) effective freedom, and the extension and deepening of democratic self-government? Or are these new governments of the 'centre-left' destined merely to tinker with the terms of established conservative political settlements or to act as reluctant agents of pro-market economic reform?

A new phenomenon?

The term 'third way' has been used to describe various innovative policy programmes, which occupy middle ground in-between two polarised positions. It may have first been used as long ago as the late nineteenth century by Pope Pius XII as part of his campaign for an alternative to both capitalism and socialism (Gould, 1998: 236). The

concept of a 'third way' has been used interchangeably with the 'middle way' popularised by Marcus Childs (1936) when contrasting the full employment and developing welfare state in Sweden in the 1930s with the Great Depression in the orthodox capitalist economies and the repression associated with Stalin's regime. In Britain, Ramsay MacDonald presented the Labour Party as a 'third way' alternative to two other possible forms of socialism, namely syndicalism and state socialism (MacDonald, 1912: 68–69). More recently, the Eurocommunist debate discussed the creation of a 'third way' between communism and social democracy, or, as Salvati (2001: 149) explains, 'between a radical revolutionary programme and the actual experience of social democratic governments in the rest of Europe'.

The concept of the 'third way' has, however, had a far wider usage. For example, the term has been utilised by Ota šik and advocates of market socialism and has been applied to Yugoslavia, under the communism of Tito, resulting from its pioneering synthesis of elements of worker participation and state ownership (Estrin, 1983). The expression also featured in the Socialist International's 1951 programme, which marked out a path distinct from both US free-market capitalism and Soviet communism (Green and Wilson, 1999: 69). More embarrassingly, for current adherents, the term was utilised to legitimise anti-democratic variants of extreme right-wing politics in the 1920s, most notably including the fascism of Franco. Indeed, the slogan 'neither right nor left' was adopted by the French fascist movement (Bobbio, 1996: 107).

Social democracy, itself, has been presented as a 'third way' between free-market capitalism and Soviet command socialism–communism (Przeworski, 2001: 312). The tendency to modify policies, strategy, ideology and even values has been a common theme running through democratic socialist and social democratic history, encompassing both Bernstein's challenge to Marxism and Crosland's championing of the Keynesian-social democratic mixed economy (Crosland, 1956; Gay, 1962). Social democracy is, in that sense, a political movement and not a fixed doctrine. Its priority is to 'build and sustain political majorities for reforms of economic and social institutions, which counter injustice and reduce inequality' (Gamble and Wright, 1999: 2). Consequently, social democratic movements have continually confronted the potential conflict between principles and power (Thomson, 2000: 20). The dynamic nature of capitalism and changes in the international socio-economic environment, together with a range of divergent circumstances produced by different national settings, further complicates matters and has caused social democrats to regularly revise their ideas and programmes

to account for new circumstances (Marquand, 1999: 10; Clift, 2001a: 55). As a result, it is perhaps not surprising that each bout of revisionism or renewal (depending upon one's viewpoint) generates fierce debate – as illustrated by the controversy surrounding discussion of the 'third way'.

The contemporary concept of the Third Way relates to the manifestation of a 'new' form of social democracy that is partly defined by contrast to a 'traditional' social democracy that has arguably lost its relevance and/or policy potency. As previously noted, this fact alone is not extraordinary, since all new social democratic strategies share the presumption that new external constraints rendered traditional strategies ineffective, and therefore new policy instruments and/or strategies had to be developed in order to maintain effectiveness and to meet new challenges (Przeworski, 2001: 312). What distinguishes the contemporary identification of Third Way from previous examples is the fact that it involves a middle way between neo-liberalism and *social democracy* itself, or at least its more traditional forms (Freeden, 1999; Tsakalotos, 2001: 38). The Third Way is, therefore, not seeking a radical middle ground between revolutionary and non-revolutionary forms of transformative socialism, nor even taking a centrist position between the extremes of communism and capitalism, but rather shifting the 'new' version of social democracy towards (but not equating with) neo-liberalism.

It is important to bear in mind that the Third Way approach is a practical phenomenon, developed to solve perceived problems from a centre-left perspective, and not derived from an established theoretical perspective. As a result, it is not surprising that such approaches vary from country to country, which makes it difficult to develop a unified theory. Nevertheless, there are sufficient elements that all variants share, to enable them to be encompassed within a common definition that embodies elements of a common strategy.

One third way or several?

The past decade has witnessed the development of a 'new' form of social democracy, which may be distinguished from a more 'traditional' version due in part to a number of philosophical differences, but predominantly because of its acceptance of many tenants of neo-liberal economics. This 'new' social democracy has perhaps been most notably identified with the fortunes of President Clinton in the USA and New Labour in Britain. In terms of the latter, responding to a devastating electoral defeat in 1983, involving 'an internationally unprecedented collapse in the popular support for the main left-of-centre party', a 'modernising'

faction sought to re-orientate the Labour Party towards its vision of a European social democratic party (Gould, 1998: 20–22). For the modernisers, the ‘project’ involved the rejection of contemporary support for unilateral nuclear disarmament, withdrawal from the European Community, public ownership and an active fiscal policy associated with a Keynesian strategy rejected as inflationary and problematic to implement due to the consequences of globalisation. The modernisation rationale was based upon

a simple thesis: Labour lost the twentieth century and allowed the Conservatives to govern for seventy of the last hundred years because it failed to modernise; it forgot the people that it had been created for. It took the modernisers to save the Labour Party. (Gould, 1998: xii)

In its place, New Labour would create ‘a dynamic capitalism’ whose benefits were experienced by *all* citizens (Rustin, 2001: 15).

The remodelling of the British Labour Party borrowed significantly from the changes that had been introduced in other progressive political parties. The primary influence was derived from the experience of the Clinton presidency of the USA, and in particular by his reinvention as a ‘New Democrat’ following the Republican electoral successes in the 1994 congressional elections (Pollin, 2001). Borrowing elements of his analysis from the Republican critique of ‘big government’ and their ‘contract with the people’, Clinton accepted the case that a New Deal social contract, based upon the co-operation of the ‘big institutions’ of state, big business and trade unions, was no longer sustainable (Corera, 1998; Meerpol, 1998; Baer, 2000; Weir, 2001). In its place, government should seek to create the conditions facilitating innovation, investment, education and training, in order to promote growth and productivity, and thereby provide jobs, rising incomes and a degree of security within a global economy (Giddens, 2000: 2). This strategy encompasses the reform of the welfare system, promoting work rather than passive receipt of benefit transfers, together with fiscal conservatism and the abdication of monetary policy to the Federal Reserve and its charismatic chairperson, Alan Greenspan (Green and Wilson, 2000: 428).

The interaction between New Democrats and New Labour facilitated the portrayal of their (largely) shared political philosophy as the core elements in a hegemonic shift in international progressive political economy. Ideological similarities were reinforced by personal links, as central British policy advisors (and later MPs) such as David Miliband

and Ed Balls had studied at MIT and Harvard respectively, and maintained close relationships with their American counterparts Larry Summers and Lawrence Katz when they were appointed to key positions within the Clinton administration (Arnold, 2000; Purdy, 2000: 184). The Third Way thus became the 'brand name' for this type of social democracy (Baer, 2000: 258–259).

The Third Way has additionally become linked with the Australian Labor Party (ALP) administrations, which governed between 1983 and 1996 under the leadership of Hawke and Keating. Their programme emphasised the deregulation of the economy in response to the challenges raised by globalisation, the adoption of non-accommodatory fiscal and monetary policies, and targeting of welfare expenditure in the attempt to promote work incentives. Consequently, they may be considered to have been a precursor of the form of 'new' social democracy that subsequently developed in North America and Europe. However, unlike the Anglo-Saxon Third Way model, the ALP predicated their approach, at least in its early phases, upon the negotiation of wage restraint via a corporatist 'Accord' with organised labour (Harcourt, 2001: 201).

This brief overview of distinctive approaches tend to accord with Pierson's (2001: 129) observation that the Third Way is typically presented with 'a peculiarly Anglophone provenance'. Nevertheless, this is to downplay the significance of similar changes and debates occurring throughout other social democratic-progressive movements, particularly in Europe. Other examples of social democratic parties adopting elements of Third Way strategy include the Spanish socialist government, 1982–1996, based upon an orthodox economic programme; the Greek Socialist Party (PASOK), whose economic programme shifted from Keynesian to a more orthodox policy stance; and elements of Italian left-of-centre coalition governments in their combination of labour market deregulation, privatisation programmes and orthodox economics (Ferreiro and Serrano, 2001; Graziani, 2001; Skouras, 2001). A Third Way mode of rethinking social democratic strategy is associated with the reform programme championed by German Chancellor Schröder, and which is expressed within the German Social Democratic Party (SPD) 'Innovation and Justice' (*Innovation und Gerechtigkeit*) programme. Moreover, Schröder and Blair published a joint paper entitled *Europe: The Third Way – die Neue Mitte*, which advanced a general framework for social democratic parties within Europe (Blair and Schröder, 1999, 2000, 2003). Elements of the Third Way are similarly found within the 'Strong and Caring' (*sterk en sociaal*) programme adopted by the Dutch Labour

Party (PvdA). Finally, the Persson administrations, in Sweden, have been closely associated with Third Way policy innovation.

Reich (1999a: 46) views the spread of Third Way ideas as evidence of the evolution of a distinctive, relatively coherent form of social democracy. Clift (2004: 49) contends that a convergence between European social democratic parties has occurred around 'new' social democratic approaches. Similarly, Sassoon (1998: 92) finds evidence of 'an unprecedented, Europe-wide convergence of the parties of the left'. The counter-hypothesis claims that 'there will never be a single Third Way, but many Third Ways' (Leonard, 2000: xx). Giddens (2000: 31, 2002: 1) distinguishes between five distinct versions of the Third Way: the market-orientated strategy pursued by New Labour in Britain; the German 'Rhineland Model' embodying a reformed version of the social market approach; the Dutch 'Polder Model' embracing both market and consensual negotiation; the reformed welfare state route in Sweden, which retains far greater continuity with previous social democratic policy and the traditional state-led programme preferred by the French socialists. Thus, although other centre-left parties tend to approximate in their policies to one or other of these positions, the significance of national contexts 'engenders enduring and significant differences between these "sister" parties' (Clift, 2001a: 71).

One significant factor underlying continued divergence focuses upon the range of conceptions of the implications of globalisation for the commitment of social democratic movements towards egalitarianism, full employment and the role of the state (Clift, 2004: 49). One indication of this may be found in the fact that, despite a degree of convergence in macroeconomic policies in European nations towards neo-liberalism, a number of key, prominent European social democrats still emphasise the potential role for Keynesian demand management, at both the national and European levels. France and Germany have proposed macroeconomic co-ordination and active aggregate demand manipulation, based upon a form of 'Euro-Keynesianism', despite the scepticism of more orthodox governments, including New Labour. Similarly, if social democrats perceive the impact of globalisation as something other than a benign and/or irresistible force, they might become increasingly attracted towards the introduction of innovative forms of the regulation of financial capital, rather than reforming their national economy to adapt to, and promote, the further intensification of international financial integration.

The practical expression of Third Way ideas depends upon other 'deeply embedded national specificities' (Clift, 2004: 49). One key factor

involves the nature of the electoral process, and primarily the propensity for social democratic parties to be able to form governments without the need for coalitions with other parties. Bergounioux and Lazar (1997: 7–8) noted that only the Portuguese socialist party, PASOK (the Greek socialists), and New Labour, out of all of the European social democratic parties, have a realistic expectation to govern without coalition partners. Coalitions involve bargaining processes, where favoured policies are traded-off against one another, and the resultant programme of government represents a compromise solution. Political parties are affected by the nature of competition with potential coalition partners (Clift, 2001a: 58), whether they are located on the Left of the political spectrum, like the Greens (as in Germany and France), former Communists (as in Italy and Sweden) and Communists (as in France), in the Centre (Germany, Italy, Sweden, Netherlands and Belgium) or representing Christian Democratic and/or Conservative viewpoints (Austria and Netherlands). Coalition government in and of itself does not necessarily imply weak government or the dilution of the particular brand of social democracy advocated in each country, as is demonstrated in the relative hegemony that the Swedish social democrats have achieved in their nation despite only having twice gained a majority of the votes in a General Election. Nevertheless, it is a further complicating factor for smaller European social democratic parties. Clift (2004: 36) summarises it thus:

‘continental social democracy’ encompasses a complex reality. Each socialist or social democratic party developed within a specific capitalist society, wedded to nation-states in various stages of democratic development, and conditioned by world wars and the scourge of Fascism. This national setting provides a set of laboratory conditions in which social democracy sought to deliver egalitarian commitments through full employment and extensive welfare states. Factors such as the nature of competition within the national party system, the financial relationship with the unions, the socio-economic structure of society, and the relative openness and competitiveness of the economy, all influence heavily the nature of each national social democratic project.

The considerable variance across Europe and the alleged lack of clear principles for key policy areas have triggered a debate on the nature of Third Way politics (Schmidtke, 2002: 4). Nevertheless, it is possible to identify a set of policy initiatives that suggest an emergent core framework associated with Third Way (new) social democracy.

Although the specific programmes instituted by each of these individual parties are by no means identical, there is enough of a common theme at their heart to identify their distinctive contributions.

A reaction to the external economic environment

The Third Way, at its heart, is derived from the attempt to develop alternative strategies to pursue many (but not all) social democratic objectives, starting from acceptance of the proposition that a number of changes in the international economic environment, within which progressive programmes must operate, have fundamentally altered the probability of successful implementation of strategies governments can employ (Skouras, 2001: 181). These include, first, the increasing significance of globalisation, secondly, the (albeit contested) conviction that flexible-specialisation forms of production will increasingly supersede Fordism and, thirdly, the replacement of Keynesianism by neo-liberal hegemony.

Third Way theorists share the perception that globalisation has undermined the attempts made by nation states to regulate and tax financial capital, trans-national corporations (TNCs), together with mobile, highly educated, managerial and professional employees. Financial market integration limits the ability of national economic autonomy, as perceptions of excessive fiscal expenditure generate fears of inflation and devaluation, and, irrespective of whether these expectations were in line with economic fundamentals, the economy in question would be likely to be penalised by rising interest rate risk premiums – a process likely to undermine economic growth. The perception of the financial markets, and the result of their subsequent actions, is likely to prove to be a self-fulfilling prophesy. The ability of the ‘electronic herd’ to discipline governments, corporations and trade unions is imposed through the cumulative effect of individual movements of physical and financial capital across the world, according to the norms established by the financial markets. Capital has increased its dominance over society due to the ‘disembedding’ of activities from constraints of time and space, whereby financial capital is instantly mobile and corporations can relocate their activities with a minimum of cost, and can therefore undermine the bargaining position of nationally located workers, suppliers and governments. As a consequence, globalisation is therefore viewed as ‘one of the key challenges for social democracy’ due to its limitation of national state autonomy, and is central to the analysis of the Third Way (Giddens, 1998a: 30–32; Arestis and Sawyer, 2001a: 5).

This view of globalisation is not universally held, and many theorists propose that most of its supposed consequences are actually caused by other phenomenon, including changes from Fordist to flexible forms of technology (Przeworski, 2001: 330). Post-Fordism implies a shift away from mass production and consumption, machinery producing standardised goods being dedicated to long runs, and unskilled workers performing standardised tasks, and towards diversified markets, multi-skilled employees operating flexible technology to produce diversified goods (Ohmae, 1990; Womack *et al.*, 1990; Amoroso, 1998: 96; Driver and Martell, 1998: 43; Scholte, 2000: 222). This view emphasises the increasing importance for business of being able to respond quickly to shifting market conditions and product demand, when operating in a business environment characterised by uncertainty in market demand and technological developments (Piore and Sable, 1984; Gustavsen, 1986; Piore, 1986). Flexible organisation structures are considered to be superior to traditional highly integrated, hierarchical alternatives with the resultant emphasis placed upon micro-level labour market flexibility – that is management autonomy over the deployment of labour within the enterprise – and a lesser concern with macro-level national labour market efficiency.

To the extent that such changes have occurred, many theorists have suggested that there is little room remaining for traditional social democratic policies (Taylor-Gooby, 1996; Pierson, 2001a: 127). Consequently, it is suggested that the state should evolve to become either a 'Schumpeterian workfare state' (Jessop, 1993, 1994b, 1995) or a 'competition state' (Cerny, 1990, 1997). Others, however, suggest that post-Fordism can sustain a variety of different regimes, including traditional forms of social democracy. Thus, the adoption of neo-liberalism is not an inevitable consequence of these changes in the productive structure (Hay, 1999: 29). Indeed, many theorists argue that the universality of the mass production regime is questionable, and therefore the transformation in production regimes is overstated (Tolliday and Zeitlin, 1986; Williams *et al.*, 1987, 1992; Hirst and Zeitlin, 1991).

Advocates of the hyper-globalisation thesis claim that it has imposed limitation upon fiscal redistribution, whilst the threat of capital flight, in an increasingly integrated international financial system, has limited or ruled out a whole range of policies previously forming a central part of a social democratic-Keynesian economic strategy (Kitschelt, 1994; Arestis and Sawyer, 2001a: 5). It is suggested that two incidents exposed the eroding ability of Keynesianism to resist the wider implications inherent within globalisation, namely the cuts in public expenditure

imposed upon the British Labour Government in 1976 (Clark, 2001), and the abandonment of a Keynesian-socialist programme pursued by the Mitterand administration in France in 1983 (Hall, 1986; Keeler, 1993; Ross, 1996; Andrews, 2001). However, it is worth noting that Clark (2001) suggests that political rhetoric over-played the significance of this moment as representing a fundamental change in macroeconomic practice. Furthermore, Cameron (1996: 58) argues that the Mitterand government retained considerably greater policy options than suggested by later neo-liberal accounts of the episode, and that it changed policy primarily because of a change in the balance of power within the governing coalition, after protracted political struggle, rather than because it was forced to do so by external constraints. Nevertheless, on occasions, the accurate determination of an event is not necessarily as important as the popular *perception* of what happened, and in both of these cases the acceptance of the inability to sustain a national, Keynesian-social democratic strategy certainly eased the rise of neo-liberalism to its present hegemonic status.

The Third Way response to globalisation necessitates government intervention to 'equip people to deal with the travails of the new risk society, in which stable employment and other traditional forms of job security can no longer be taken for granted' (Corera, 1998: 14). This involves the provision of life-long education and training programmes that facilitate the adaptation of individual skills to a dynamic labour market, together with a modified welfare system providing portable benefits (i.e. pensions, health care) due to the necessity for frequent job changes. In addition, the Third Way strategy requires the creation of a favourable environment for transnational investment, whether through lowering general taxation, generation of a more flexible and highly skilled labour force, deregulation of the economy, providing monetary incentives to encourage inward Foreign direct investment (FDI) and so forth (Arestis and Sawyer, 2001a: 6).

The freedom of action governments enjoy may have been reduced by globalisation, but autonomous action remains possible. Most investment is domestically financed, and even where FDI is a significant element of capital formation, it is more closely associated with access to profitable markets, access to skilled labour and the absence of economic and political instability, and is relatively insensitive to government policies in general. Similarly, although financial globalisation has increased the constraint upon economic policy autonomy posed by the likely reaction of investors to government policies, the factors determining capital flows are difficult to determine and often have multiple equilibria

(Przeworski, 2001: 330). Under normal circumstances, a rise in interest rates should increase inward capital flows in search of higher returns. However, if it causes increased expectations of an imminent devaluation, it may have the opposite effect, circa the ejection of Sterling and the Swedish krona from the European Exchange Rate Mechanism in 1992.

Nation states remain the most powerful actors in the international economy due to their ability to determine the conditions pertaining to economic activity within the boundaries of their territory. TNCs do not control territory, legitimate military force and nor do they have the ability to make laws or design the apparatus needed for their implementation. Governments have the ability to regulate economic activity and introduce taxation, such as a 'Tobin tax'¹, in the attempt to steer the behaviour of private economic agents. As a result, Giddens (1998a: 30–32) accepts the proposition that national government remains strong, has not been rendered impotent by globalisation, and retains the ability to impose its priorities upon global capital through transnational collaboration. However, supporters of the Third Way wish to utilise transnational regulation to maximise gains from increased trade and capital flows, in terms of a predicted enhanced rate of growth, optimum allocation of scarce resources, and facilitating the development of the Asian sub-continent, whilst limiting less palatable consequences such as increased unemployment and rising inequality. Thus, Giddens (2000: 159) argues that, 'taking globalisation seriously means emphasising that democratisation cannot be confined to the level of the nation state', thereby reinforcing support for supra-national institutions, such as the EU, to provide a focus for progressive response to globalisation.

Rojas emphasises 'the unparalleled advances of the past 30 years' to substantiate his belief in the 'enormous potential' of the global economy to alleviate underdevelopment, and that therefore government policy should be to 'transform more and more countries into dynamic parts of this expansive economy' (Rojas, 1999: 12). Instead of opposing further extension of globalisation, Third Way proponents suggest that supranational authorities could concentrate upon the surveillance of financial transactions, to prevent destabilisation caused by excessive capital flows, together with the provision of international liquidity to facilitate the expansion of the world economy (Giddens, 2000: 126–127).

Pro-market philosophy and the restricted role of the state

The Third Way takes a markedly different approach to the role and scale of the state than traditional social democracy, which has generally favoured its expansion into social and economic matters in order to

create new policy instruments and thereby more efficiently enact social democratic strategy. The state has therefore been viewed as the principle instrument for the redistribution of income and power, the regulation and taming of capital, together with the ability to better manage the capitalism to produce full employment, rapid growth economy (Padgett and Paterson, 1991: 49).

Neo-liberal critics of the 'big state' have argued that it has become too impersonal, threatens individual liberty and is less efficient than market forces. Consequently, state activities should become limited, and its size dramatically reduced, in order to free resources for more efficient market allocation. In this debate, Third Way theorists adopt a position closer to the neo-liberals, in that they favour reconstruction of the state in order to create 'the state without enemies' (Giddens, 1998a: 70).

This approach shares with the neo-liberals their criticism of an over-expansion in state power leading to moral hazard, dependency, reduction in incentives, bureaucracy, 'clientism', fiscal irresponsibility, a tendency towards authoritarianism and a lack of accountability, even potentially corruption and fraud. As a result, Third Way literature promotes the idea of freezing at its present level, or reducing, the scale of the state through engineering a decline in the ratio of public expenditure as a proportion of GDP (Giddens, 2000: 7; Arestis and Sawyer, 2001a: 6).

In place of the 'strong state', Third Way philosophy relies upon an optimistic conception of the ability of the civil society to act as a 'self generating mechanism of social solidarity', and in the process reducing the need for the state to form a conduit for corporatist frameworks (Giddens, 1998a: 11). Nevertheless, this does not imply a total disregard for the state to play a positive role in the new Third Way economy (Rustin, 2001: 22). Indeed, the state is expected to swap its activist Keynesianism for a role as a 'social investment state', providing education and training programmes in order to enable individuals to gain the skills and abilities they need to successfully compete in the global labour market.

Redefining education and labour market policies as human capital investment narrows conception of the benefits arising from this expenditure, but it does provide a financial case for certain types of increased spending. By inference, however, it condemns other areas of public provision to a continual tightening of resources and cutback in provision in the absence of hard-won productivity gains. Similarly, the reform of the welfare state is intended to strengthen a drive to get people into work, by increasing incentives, and thereby reducing social

exclusion (Tsakalotos, 2001: 39). Giddens (2000: 6) describes this change in emphasis as one where 'the state should not row, but steer: not so much control, as challenge'.

Macroeconomic strategy

The economic strategy advocated by Third Way theorists involves a rejection of the Keynesian policies required to pursue full employment, and their replacement with an 'iron commitment to macroeconomic stability and financial prudence' (Routledge, 1998: 222). Government no longer utilises all of the economic policy instruments under its control in order to pursue multiple objectives simultaneously, the most important of which being to maintain the full employment of all resources in the economy. One additional feature of the Third Way approach is a marked preference to discuss targets of 'high' rather than full employment. Indeed, Giddens (1998a: 126) rather pessimistically suggests that this may be a rational response to his perception that global capitalism no longer generates sufficient work to accommodate a full-employment strategy. Instead, it seeks the creation of a stable framework for business activity, implying price stability having become the new principle goal of economic strategy (Gould, 1998: 244; Tsakalotos, 2001: 33). Government activism is restricted to supply-side policies aimed at improving the 'employability' of the unemployed and thereby enhancing their capability to compete for jobs created in the new flexible labour market (Blair, 1998d; Finn, 2000: 386).

The Third Way economic programme is built upon the acceptance of a number of theoretical positions, either consciously or in ignorance of the finer points of the economic literature. For example, the replacement of full employment by low inflation as the principle goal of macroeconomic strategy, together with a passive fiscal stance and the detachment of monetary policy from a co-ordinated policy stance, suggests an acceptance of the natural rate of unemployment hypothesis. This holds that unemployment is ultimately determined by structural factors, such as the wage flexibility of the labour market, rather than the result of aggregate demand. Thus, the Phillips curve trade-off between lower unemployment and higher inflation is rejected, with the inference that governments which seek to lower the unemployment rate below the natural rate can do so only temporarily and at the cost of faster rising prices. Hence, the policy solution is for governments to deflate the economy to lower prices, since market clearing theory will have at worst only a temporary impact upon output and prices, because these

are determined in the labour market, not by aggregate demand. Unemployment should instead be tackled by measures such as reducing the generosity of benefits and the length of time they are paid, introducing inspection regimes upon the economically non-active – to help reduce job search time and deter fraud – reduce the power of unions to push up wages and hence increase unemployment, together with the introduction of tax incentives for low-paid work, and so forth.

This is a theoretical and policy stance associated with the monetarist and New Keynesian schools of economics – the latter representing a synthesis of neo-liberalism and elements of Keynesian policy activism in the short run. This is a position that causes most post-Keynesians to regard New Keynesianism as ill-defined and not forming part of the body of thought associated with Keynes, Kaldor, Robinson and Kalecki.

Fiscal policy

Fiscal policy becomes a largely passive economic instrument under the Third Way, ensuring that a tight control is kept upon public expenditure. This is kept constant in real terms such that it declines as a proportion of national income as the economy grows. There is no concept of the need for management of aggregate demand, either through a process of ‘fine tuning’ or even ‘coarse tuning’. The Third Way approach is therefore based upon the Say’s Law hypothesis, assuming that the economy always tends towards the full employment of its resources because economic activity is set by the supply side of the economy and the level of effective demand adjusts to the appropriate level. This view holds that the economy is relatively stable and any shock, which does cause a temporary deviation from full employment equilibrium, will be self-adjusting through price flexibility rather than via variations in output and employment. Consequently, the budget should be balanced over the economic cycle, and counter-cyclical policy is not required, save for the operation of automatic stabilisers during a temporary downturn in activity.

Monetary policy

Monetary policy is dedicated to meeting the new prime objective of price stability, rather than undertaking a more balanced role in stabilising the domestic economy, complete with full employment and a favourable rate of growth. Moreover, there is an increasing tendency, particularly within EU member states, to transfer monetary policy into the hands of an independent central bank (CB). The motivation behind this policy initiative was advanced by a relatively new development in the literature

which purports to demonstrate that, removed from government control, central bankers can and will be successful in targeting lower inflation (Rogoff, 1985). However, there is a considerable danger in placing one of the most important macroeconomic policy instruments into the hands of central bankers, whose preferences are likely to be more 'conservative' in terms of their preference for very low rates of inflation irrespective of the impact upon growth rates and unemployment. The evidence supporting this change is statistically weak, and there is almost as much data to predict that independence would result in relative economic stagnation (Cukierman, 1992; Posen, 1995).

Labour market programmes

The supply-side orientation of Third Way policy places great emphasis upon the labour market, in terms of reducing unemployment and ensuring that wage formation is consistent with low inflation targets. This approach concentrates upon increasing the incentives to work, through time-constraining benefit entitlement and transferring the emphasis to minimum wages paid in employment, together with enhancing the skills and abilities of individual workers. It ignores the major contribution played by aggregate demand, and the evidence that employment is directly associated with productive capacity. This is due to the adaptation of these policy proposals from within a neo-liberal framework, when the level of employment is assumed to be determined by Say's Law. This proposes that supply will create its own demand, as opposed to the Keynesian concept of government intervention typically being necessary to prevent demand deficiency resulting in unemployment and productive capacity laying idle. Consequently, the Third Way strategy is based upon a non-Keynesian theoretical base – one that roots all the problems of unemployment, a poor level of investment and industrial growth, low growth rates and social inequality, as originating within the labour market.

One Third Way solution involves the re-skilling of the labour force, through an expansion in educational and training programmes to make the unemployed more employable. Much of this analysis is based upon the work of Richard Layard, who argued that the main thing that determines the number of jobs is the number of employable people in the economy rather than adjusting the level of aggregate demand. Furthermore, a more educated pool of labour, better fitted to the job vacancies being advertised, reduces supply bottlenecks in the economy and thereby lessens the inflationary pressure generated by employers raising wages to attract scarce labour. It focuses upon the problems of

long-term and youth unemployment, in addition to seeking to curb tendencies towards 'Eurosclerosis', whereby an overdeveloped welfare state reduces incentives to work and hence is associated with rising unemployment and falling rates of growth (Nickell, 1997; Siebert, 1997).

As human capital is regarded as the major driver of economic growth in the information age, this element of Third Way thinking is in line with the new endogenous growth theories, which claim to have found evidence that long-term economic growth rates are closely associated with a nation's combination of both physical and human capital. Therefore, educational expenditure should make a positive contribution towards enhancing the growth rate (Harcourt, 2001: 215). The welfare state should, then, be reconstituted into a 'social investment state' precisely for this purpose (Giddens, 2000: 52).

Retraining programmes can help to reduce a skills mismatch, but are powerless to correct demand deficient unemployment, which the European economy has arguably been suffering for over a decade (Arestis and Mariscal, 1997; Stockhammer, 2004a). Thus, Solow (1998: 30–31) claims that, in the absence of near full employment, retraining programmes may result in the retrained unemployed competing with low-skilled workers in employment, leading to a fall in related wages and may, therefore, encourage employers to replace semi-skilled workers with the now more competitive, less skilled alternatives.

Industrial relations

It is difficult to identify a distinctive Third Way approach to industrial relations. Concertation and wage bargaining co-ordination remain significant features of many European member states. Others have experienced a degree of decentralisation of wage bargaining. Whilst other nations have a markedly firm- or individual-centred approach to wage formation. Moreover, even within specific national programmes, dualistic tendencies can be noted. For example, New Labour emphasises the notion of social partnership between employers and trade unions, together with adopting the EU minimalist social dimension, yet simultaneously they champion the deregulation and flexibilisation of the labour market. This dualism may be at least partly explained by the clash between the remnants of previous 'old' Labour policy and a predominantly neo-liberal New Labour programme (Undy, 1999: 333). Thus, the New Labour strategy may be far more neo-liberal than the trace elements of a previous policy stance would make it seem, at first glance.

Social policy reform

The Third Way approach to social policy centres upon the belief that employment is the only secure and sustainable means to social inclusion (Rustin, 2001: 20). It concentrates upon the expansion of individual opportunities, which can be maximised through work and a programme of continual re-skilling, rather than the redistribution of income and wealth. It promotes equality of opportunity, but says little about the inequality of outcomes and the obstacles within society preventing many from taking full advantage of the opportunities on offer (Faux, 1999).

Social policy reform is perceived as providing a potential contribution towards the Third Way work-centred programme through a reduction in the level of payment and duration of unemployment benefits, together with an improvement in take-home income when in work. Layard *et al.* (1991) found that these features were associated with higher unemployment, through a reduction in work incentives. Moreover, Giddens (1998a: 122) suggested that high levels of unemployment are linked with the provision of 'generous benefits that run on indefinitely and to poor educational standards at the lower end of the labour market – the phenomenon of exclusion'. Consequently, Third Way policies tend to include an element of benefit reduction – whether through the British government's practice of uprating in line with prices and not average wages, or through actual cuts in entitlements. Hence, increased reliance upon national minimum wages, together with the introduction of tax credits modelled upon US precedence, has tended to provide greater incentives for individuals and families to seek employment, even if it is low skilled and low paid (Arestis and Sawyer, 2001b: 52–56). Undy (1999: 332) argues that this second element, namely the targeted schemes to boost the disposable income of low-paid workers, distinguishes the Third Way strategy from neo-liberalism.

The development of the welfare state was one of the proudest achievements flowing from traditional social democracy. Indeed, utilising a concept most closely associated with T.H. Marshall, the welfare state has been presented as part of a gradual extension of citizenship rights from legal and political rights to social and ultimately economic rights (Marshall, 1963). In this regard, the welfare state decommmodified labour and thereby provided individuals with enhanced choices about how to live their lives (Esping-Andersen, 1990). Giddens (2000: 103), however, argues that this approach has become unsustainable, both in terms of cost and fundamental concept. Welfare programmes create dependency and introduce moral hazard through the provision of perverse incentives (Giddens, 1998a: 115). Therefore, instead of seeking to insulate and protect

individuals *from* the consequences of market mechanisms, the Third Way aims to enhance the position of individuals *within* the global market system.

Achieving fundamental reform of the welfare system is not easy to achieve due to the reliance of entrenched interest groups upon welfare transfers. However, Giddens (2000: 104) points to the development of new social tensions, including taxpayer resistance to further growth in public expenditure, differences between generations relating to the generosity of the welfare system and conflict between those who benefit from the system and those who are net contributors, all of which increases the possibility of forming coalitions for reform. For example, New Labour Prime Minister, Blair claims that with more than £50 billion currently allocated through social transfers to people of working age, his 'greatest challenge' will involve the 'welfare to work' programme, which aims to 'refashion our institutions to bring the new workless class back into society' (cited in Finn, 2000: 388).

One obvious consequence of the Third Way approach to welfare reform relates to the impact this is likely to have upon the distribution of income. Measures to increase employability and the provision of minimum wage legislation have equalising effects upon the national distribution of income, whilst the promotion of low-paid jobs, reduction in benefits relative to average wages and displacement of progressive by indirect forms of taxation, all have regressive effects (Atkinson *et al.*, 1996: 225–256). In the absence of progressive income redistribution, Tobin (1999) states that 'one generation's inequality of outcome is the next generation's inequality of opportunity'.

European integration

The Third Way strategy amongst European economies is identified closely with the process of European integration. Part of the reason for this is due to the neo-liberal foundation that has been established for the single internal market (SIM) and economic and monetary union (EMU) that are forming the basis for the 'new' European economy (Whyman, 2001). In particular, the Stability and Growth Pact (SGP) maintains and reinforces the convergence conditions created to ensure fiscal conservatism amongst potential EMU participants, and which has contributed to a decade or more of economic stagnation across the majority of the European continent (Holland, 1995; UNCTAD, 1996).

The policy framework embodies a distrust of politicians to successfully manage economic policy, so that the supranational European Central

Bank (ECB) has been created wholly independent of all democratic influence and/or control, and there has been no comparable European Ministry of Finance created to counter its dominance over the European economy. The ECB's sole policy objective is price stability, which it defines within a range of 0–2 per cent, and the bank is instructed to avoid all consideration of other factors, such as employment and growth, if these detract from meeting this objective. Thus, there is no balanced portfolio of macroeconomic goals established for the new Europe, only the monetarist preoccupation with low inflation, assuming a natural rate of unemployment and the policy ineffectiveness of Keynesian counter-cyclical intervention.

Tsakalotos (2001: 38) argues that the EU macroeconomic strategy should not be considered to be a purely neo-liberal approach due to its championing of the social chapter and the fact that social partnership in the industrial relations sphere has been retained in many member states. However, these facts are equally consistent with the proposal that the economic stance is inherently neo-liberal, but that the social policy advocated by the EU Commission enhances the primacy of federal determination over wider areas of formally national policy, and with it the role and importance of the Commission itself. The social chapter is, at best, a minimalist construction, whose operation is in many respects in contradiction to the overall neo-liberal economic structure created at Maastricht (Whyman, 2001). Moreover, the social partnership maintained by many nation states is restricted to ensuring a social consensus for contentious cuts in welfare programmes, due to the requirements of the SGP, and/or the moderation of real wages to facilitate a transition to EMU. Furthermore, suggestions that the EU might provide the necessary economic muscle to introduce a form of Euro-Keynesianism is neither very likely within the present institutional arrangements, and nor is this an example of Third Way thinking, because advocates of this initiative are more readily associated with 'traditional' forms of social democracy.

Critique of the Third Way

The Third Way has attracted a considerable amount of criticism. For example, Faux (1999: 75) describes it as 'an intellectually amorphous substance' with parameters 'so wide that it is more like a political parking lot than a highway to anywhere in particular'. *The Economist* (1998: 49) remarked upon its 'fundamental hollowness', whilst Hall (1998) dismissed it as 'the great moving nowhere show'. Rustin (2001: 13)

suggests that the version of the Third Way being developed by New Labour in Britain was initially a concept discussed by political strategists, before only latterly being provided with any theoretical foundation. In practice, he claims that this has provided a political platform, which closely mirrors the failed agenda associated with the now defunct SDP of the 1980s. Marquand (1998: 19) agrees that it is 'patently not socialist... not even social democratic or social liberal'.

Ryan (1999) claims that the approach contains little original analysis, as it adopts many ideas from the form of 'New Liberalism' that existed in Britain at the beginning of the twentieth century. Furthermore, Green and Wilson (2000: 428) suggest that it is intended to 'legitimate a seismic shift in social democratic policy towards neo-liberalism'. This viewpoint is disputed by White (1998: 18–21). He claims that, although it is vague in terms of detailed analysis, the Third Way strategy combines individual opportunities and civic responsibility in such a way that it promotes an 'asset based egalitarianism'. Finally, Giddens (2000: 22–25) cites criticisms that the project is 'amorphous', lacking direction, ignores environmental issues and has no effective economic programme apart from an uncritical adoption of neo-liberalism and the promotion of marketisation.

Power and social class

One powerful criticism of the Third Way approach is that it is too accepting of the existing structures of power within capitalist society, and that it appears to consider that there are few (if any) conflicting interests which cannot be reconciled (Hall, 2003: 84). Marquand (2003: 84) states that '... the Third Ways discourse... is disconcertingly devoid of any sustained reference to power'. For example, Giddens does not allow for the market being a principle means of widening social inequality (Finlayson, 1999: 76). Moreover, the fact that the Third Way prefers to focus upon social exclusion rather than inequality represents a limitation of analysis and a reduction of traditional social democratic objectives (Tsakalotos, 2001: 41). In addition, it also ignores the Kaleckian argument that capitalism may be incompatible with sustained full employment in the absence of corporatist-institutional reform, due to the fact that tight labour markets empowers labour, reduces the impact of industrial discipline and is likely to be opposed by organised capital (Kalecki, 1943; Henley and Tsakalotos, 1993).

Giddens' (2000: 37–38) counter-argument states that 'the struggle to sustain and extend democratic mechanisms, control corporate power, and protect cultural minorities is fundamental to the third way, as it

has been to previous forms of social democracy'. However, this point sits awkwardly with his later argument, that:

The division between left and right reflected a world where it was widely believed that capitalism could be transcended, and where class conflict shaped a good deal of political life. Neither of these conditions pertains today. (Giddens, 2000: 39)

Wood (2001: 49) argues that the Third Way has adopted a 'benign view of social organization' that contrasts with both traditional social democracy and neo-liberalism, because as the former emphasised class conflict and neo-liberalism atomistic individuals, the Third Way is based upon the notion of 'individuals laden with both rights and responsibilities to communities'. Crouch (2001: 106) suggests that New Labour views concepts of class conflict as 'old-fashioned' and claims to have transcended a society stratified by classes, with fundamentally antagonistic interests engaged in zero-sum conflicts over the distribution of resources. Instead, its preference is to visualise society to be comprised of communities of mutual dependence, where consensus can be reached to pursue mutual interests simultaneously. However, this stance is criticised as naive or duplicitous. Hutton (2003: 118) argues that this element of the Third Way has enabled the state to reduce its social obligations and shift burdens onto 'those least able to bear it'. Similarly, Crouch (2001: 106) notes that the globalised, deregulated economy has facilitated greater capital autonomy, whilst simultaneously organised labour has become increasingly fragmented and lost a degree of coherence. Indeed, Crouch (2001: 106) claims that 'this is not a transcendence of class conflict but a particular turn in its development: a forceful reassertion of the dominance of one class'.

Economic democracy

The Third Way places great emphasis upon an active civil society providing a viable constraint upon the power of both markets and governments (Giddens, 2000: 64). However, Marquand (1997: 336–338) suggests that this vision is notably narrower than the traditional social democratic promotion of 'citizen empowerment', in that:

The citizenship ideal is one of participation, activity and self-development and, by the same token, of accountability, transparency and scrutiny. Good citizens debate, argue and question; they don't simply accept what is handed out to them. And they cannot switch

off their citizen selves when they go to work. That, of course, is what the early social democrats meant by social democracy. A democracy confined to the political sphere was no democracy; it had to embrace the social sphere as well. Citizenship was indivisible.

In addition, the Third Way project has little or nothing to say about the traditional social democratic demand for economic democracy; in other words, extension of democratisation from the social to the economic sphere of activity (Tsakalotos, 2001: 41). The promotion of employability as a means of empowerment of individual workers in the global labour market is an individualistic and distinctly different concept to the previous social democratic notion of economic citizenship through collective organisation and labour market institutions. Furthermore, the Third Way is almost completely silent upon the potential of social ownership to further social and economic goals associated with social democracy. Instead, government regulation of private sector corporations is the preferred option, based upon the neo-liberal assumption that private ownership will inevitably lead to greater efficiency.

Is it social democracy?

Giddens (1998a: 26) claims that the Third Way represents an attempt to 'transcend' neo-liberalism and 'old-style social democracy' by providing a 'framework of thinking and policy-making that seeks to adapt social democracy to a world that has changed fundamentally over the past two or three decades'. Indeed, social democracy once provided an alternative to command communism and free-market capitalism, combining a concern for equality, social solidarity, social protection and full employment, with democratisation, economic efficiency, together with the combination of regulated capital and the social ownership and control of resources (Glyn, 2001: 3; Rustin, 2001: 12). However, Dahrendorf has subsequently announced the 'end of the social democratic century', whilst Giddens claims 'the death of socialism', and therefore that social democracy has lost its ability to transform society because 'no one any longer has any alternatives to capitalism' (Giddens, 1998a: 3, 43, 2000: 19–20).

The rise of globalisation and subsequent decline of national economic self-management, together with the growth of post-Fordist production and with it the homogenised working class, have weakened the Keynesian-social democratic paradigm. Uncertainty arises concerning whether traditional social democracy methods retain the ability to deliver desired objectives. However, the solution advanced by

the Third Way is to reject those traditional goals it cannot in any case achieve because of the inadequate policy instruments instigated according to its neo-liberal foundations. Thus, full employment becomes regulated to a long-term aspiration, equality is restricted to opportunity and not outcome, whilst social policy is defined in terms of reducing social exclusion through the promotion of low-paid employment opportunities.

The democratic control over a citizen's own life has become a non-issue, with even the democratic control over national macroeconomic policy reckoned to be suspect due to acquiescence to capital mobility and acceptance of the EU's neo-liberal economic regime. Indeed, Arestis and Sawyer (2001b: 58) claim that the macroeconomic stance pursued by leading Third Way regimes, including the New Labour government, can be perceived as the 'final triumph of (new) monetarism and the defeat of Keynesian economic policies'; at least, if not challenged by a renewal of the post-Keynesian-social democratic synthesis. Therefore, it is an interesting question as to whether the Third Way approach is really a modernised version of social democracy, or a new phenomenon, more closely related to classic political liberalism. This is one of the questions that this book will seek to answer.

Note

1. For further discussion, see Chapter 9.

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